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"The Impact of the Foreclosure Crisis on Public and Affordable Housing in the Twin Cities"

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Thank you Chairwoman Waters, Ranking Member Capito, Congressman Ellison and members of the subcommittee for inviting me to testify before you, today. Today's discussion is an important one, given the complex changes our housing market has undergone over the past two and a half years, the new challenges we face as a result of the housing market turmoil and foreclosure crisis, and the structural challenges which have persisted through collapse and this current period of stabilization. My testimony will address the current state of the U.S. rental housing market, the impact of the foreclosure crisis on the rental market, including the local market here in Minneapolis, HUD's efforts to stabilize communities impacted by the foreclosure crisis and restore leadership in delivering rental housing assistance to low-income Americans.

Rental Housing Affordability across the Nation and in the Minneapolis-St. Paul Region

Recently, well-publicized national indicators have pointed to increasing stress in the U.S. rental housing market. Vacancy rates are on the rise as a result of dampened demand and additional supply repurposed from the ownership market. Spreads between asking rents and effective rents are widening, asking rents are now $65 higher than effective rents (6.6% of the effective rent) - the largest gap over the past four years. While some new renters have been the beneficiaries of this softness, drawing concessions from distressed property owners, the budgets of many more low-income renters have been strained as household incomes fall, as a result of unemployment and lost hours worked. Softness in the broader rental market has not substantially eased affordability concerns for low-income renters. Loss of income stemming from the recession is likely offsetting affordability gains from declining rents. Vacancies in HUD's assisted stock remain considerably lower than market levels, and the number of cost burdened low-income renters is on the rise. Based on estimates from the 2008 American Community Survey, 8.7 million renter households paid 50% or more of their income on housing, up from 8.3 million renter households in 2007.

Speaking in terms of a single national housing market ignores important nuances underlying the national picture. The cost of shelter burdens households differently across markets. Tight market conditions, created by constrained supply and strong demand, in communities such New York, Los Angeles and San Francisco strains affordability for renters up the socio-economic ladder. In other markets, affordable housing for low and moderate income renters is more readily available, but is often located in neighborhoods with the highest concentrations of poverty and the least economic opportunities. Persistent across virtually all housing markets in the U.S. is a shortage of rental housing units that are affordable and available to extremely low-income renters. The American Housing Survey indicates there are as few as 44 affordable and available units per 100 extremely low-income renters in the U.S. [1]

In the Minneapolis-St. Paul Metro area, housing affordability for extremely low-income households is similarly scarce. Extremely low-income households are those earning less than 30% of the Area Median Income, or approximately $25,000 for a family of four. The shortage of affordable and available units for extremely low-income in the Minneapolis-St. Paul metro region mirrors the national shortage.[2] However, for low and moderate-income renters, the Minneapolis-St. Paul region remains considerably more affordable than similarly sized coastal metros. While there appears to be no absolute shortage of rental units affordable to households earning more than 30% of the Area Median Income, the availability of affordable rental housing in safe, opportunity-rich communities remains a concern.

Recognizing that rental affordability at the low-end of the rental market is a crucial challenge for the nation and its many housing markets, HUD has reasserted a leadership role as a catalyst for expanding the availability of decent and affordable rental housing. If this crisis has taught us anything, it's that this nation needs a balanced, comprehensive national housing policy – one that supports homeownership, but also provides affordable rental opportunities, and ensures that nobody falls through the cracks. Our 2010 budget restores much needed balance to the nation's

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[1] Data Source: American Housing Survey National Sample 2007

[2] PD&R tabulations of American Community Survey Public Use Microdata Sample (PUMS) 2008; HUD 2008 Income Limits

Note: Figures are adjusted for household size as well as the number of bedrooms, reported here for the Minneapolis-St. Paul-Bloomington, MN-WI Core-Based Statistical Area housing policy. Since our policies do not operate in a vacuum, it is important to consider how rental housing is impacted by broader housing market dynamics.

Foreclosure and Rental Affordability

The relationship between this foreclosure crisis and the dynamics of our rental markets are not well understood, even by housing experts. It is particularly difficult to untangle the impact of foreclosure from broader recessionary effects. There is considerable anecdotal evidence and some quantitative evidence suggesting that families who experience foreclosure are opting to "double up" with friends and relatives, thereby depressing demand in the rental market and potentially contributing to rising vacancies. This "doubling up" may be an important short-term transitional fix to avoid homelessness, but poses serious concerns about overcrowding if these households are unable to find affordable rental housing down the road. In the short term, many households who have gone through foreclosure will be better suited as renters and will need an affordable rental option. The net impact of the foreclosure crisis on the affordable rental housing stock is still unclear. In the same way that foreclosures on single-family properties have created a shadow inventory of homes in the REO stock of financial institutions, foreclosures on multifamily properties have removed existing rental properties from the available rental supply. However, there have also been additions to the rental stock from newly constructed units originally intended to be condos and the conversion of other condominiums back to rental units.

In the Minneapolis-St. Paul area, a substantial portion, nearly 20 percent, of the rental stock is in single-family homes, and another 12 percent of rental units are in 2-4 unit buildings. [3] Research from the Humphrey Center at the University of Minnesota suggests that as much as 60 percent of buildings with foreclosures in 2006 and 2007 were renter-occupied. [4] Recognizing the tumultuous experience these renters face during foreclosure, Congressmen Ellison introduced and President Obama signed into law the Protecting Tenants at Foreclosure Act in 2009. This Act protects renters in foreclosed properties by allowing them to fulfill their lease, unless the property is sold to a purchaser occupying the unit as a primary resident. Additionally, tenants must receive a warning at least 90 days in advance of an eviction notice. Also assisting renters, the Neighborhood Stabilization Program (NSP) funds *can and are* being used to support the creation of rental units.

Rental affordability is a key priority of Secretary Donovan, but HUD also remains focused on restoring stability to the nation's housing market. First through Recovery Act funding, and continued in the 2010 budget, HUD is creating jobs, making homes more energy efficient and stabilizing neighborhoods, while laying a new foundation to make America competitive in the 21st century economy. I'd like to describe how HUD's investments through the Neighborhood Stabilization Program are strengthening and stabilizing neighborhoods in Minneapolis as well as across the country.

Neighborhood Stabilization Program Funding

[3] Data Source: American Community Survey 2008
[4] Ryan Allen "Unraveling the American Dream: Foreclosures in the Immigrant Community of Minneapolis." Humphrey Institute for Public Affairs, University of Minnesota, March 2009.

The first round of the Neighborhood Stabilization Program (NSP1) was authorized under HERA in 2008. Through NSP1, HUD allocated $3.92 billion to 309 states, territories, and local governments to help stabilize communities that have suffered from significant foreclosures and abandonment. The funding distribution was based on a formula allocation.

NSP funds may be used for a range of activities that include, but are not limited to:

- Establishing financing mechanisms for the purchase and redevelopment of foreclosed homes and residential properties;
- Purchasing and rehabilitating homes and residential properties abandoned or foreclosed;
- Establishing land banks for foreclosed homes;
- Demolishing blighted structures; and
- Redeveloping demolished or vacant properties.

While NSP1 did not specify if the units produced or preserved through activity be rental or owner-occupied, it did mandate that at least 25 percent of the funds appropriated be used to assist individuals or families whose incomes do not exceed 50 percent of the area median income. In addition, all activities funded by NSP must benefit low- and moderate-income persons whose incomes do not exceed 120 percent of area median income.

In 2008, HUD awarded the State of Minnesota, the cities of St. Paul and Minneapolis, and Anoka, Dakota, and Hennepin counties more than $57 million in NSP1 funding. About 52 percent of units that are expected to be preserved or produced by Minneapolis's NSP1 funding will assist households making at or below 50 percent of the area median income. Approximately 26 percent of funding awarded to the State of Minnesota is expected to serve low-income households, earning at or below 50 percent of the area median income.

The American Recovery and Reinvestment Act of 2009 authorized HUD to administer an additional $1.93 billion in NSP funding, commonly known as NSP2. Last week, the Secretary awarded the City of St.-Paul $18 million in NSP2 funds. The City of Minneapolis was awarded $19.5 million in a consortium agreement with City of Brooklyn Park Community Development Department, Hennepin County Housing Community Works, and Transit Department. This region's approach to neighborhood stabilization is a model of coordinated, cohesive community development that makes efficient use of existing housing development capacity and sets a high bar for providing jobs and other benefits for members of the affected communities. Working in partnership with the Twin Cities Community Land Bank LLC, an affiliate of the Family Housing Fund created in May 2009, these jurisdictions have launched an innovative approach to using their NSP 1 and NSP 2 allocations that utilizes the Land Bank as an intermediary to identify, purchase and coordinate the disposition of foreclosed properties to a pre-identified group of nonprofit developers as well as the City of Minneapolis. To tap private market resources, the Land Bank also is working with responsible for-profit developers that are engaged in community revitalization efforts in the City of Minneapolis. Last October, my office of Policy Development and Research highlighted land banks as a tool to addressing foreclosures in report called "Revitalizing Foreclosed Properties with Land Banks.". With additional funding leveraged from private and philanthropic sources, the Minneapolis-Brooklyn-Hennepin Consortium will use 25% of their NSP2 funding to support households at or below 50% of the area median income.

Impact of Foreclosures on Renters in Connection with other HUD programs

Historically public housing authorities have had little role in the foreclosure crisis. However, a new program allows PHAs to acquire HUD REO foreclosed properties and either convert them to rental properties or sell them through the Section 8 Homeownership program, which allows

Section 8 renters to apply their vouchers to monthly homeownership costs like mortgage payments and maintenance expenses. This program is currently being offered in many of the Gulf states, but not Minnesota.

HUD's multi and single family mortgage insurance programs do not show much activity in the interaction of renters and foreclosures. There are currently no foreclosed HUD insured multifamily buildings in Minneapolis. Indeed, in the past two years there has only been one completed foreclosure on a HUD insured multifamily building in Minnesota. However, there are three projects in Minnesota that have recently initiated foreclosure proceedings, which are located in Duluth, Granite Falls, and Brooklyn Center, a suburb of Minneapolis.

In the unlikely event of a foreclosure on HUD insured multifamily properties, HUD determines the use and affordability restrictions for the buildings once HUD sells the properties. In order to preserve affordable housing, HUD mandates that the purchaser maintains the property as rental housing with affordable rents to households earning at or below 80 percent of the area median income for 20 years. The purchaser must also renovate the building to meet HUD standards, including removing any lead-based paint, asbestos or mold hazards. Finally, the purchaser cannot discriminate against prospective tenants with Section 8 vouchers and must maintain any existing Section 8 HAP contracts.

Of the 100,000 single family mortgages HUD insures in Minnesota, HUD has acquired only 719 homes as a result of a foreclosure. Forty of these so-called "HUD Homes" are located in Minneapolis, twenty of which are under contract to sell. HUD is aware of delays in sales of some of the HUD Homes in the Minneapolis area. Our Office of Single Family Asset

Management is working with its contractor to improve the contractor's performance and the face it presents to prospective buyers of these homes.

While these homes may include up to four units, it is highly unlikely that renters have been significantly impacted by these foreclosures. While in inventory, HUD Homes that were previously owner-occupied are usually not rented out, nor does HUD sell them as rental properties because the primary objective of the single family property disposition program is to expand homeownership opportunities, strengthen neighborhoods, and to ensure a maximum return to the mortgage insurance fund, as determined by HUD in 24 CFR 291.1(a)(2).

> *"The purpose of the property disposition program is to dispose of properties in a manner that expands homeownership opportunities, strengthens neighborhoods and communities, and ensures a maximum return to the mortgage insurance funds."*

FHA and HUD's Office of Community Planning and Development are coordinating activities to prioritize HUD Homes for NSP grantees. This includes mapping FHA foreclosures over NSP 1 and NSP2 target areas to help grantees prioritize the purchase of these homes The HUD Homes program features a "priority period" for most sales, during which the home is made available only to purchasers who will occupy the home as their primary residence, Establishing this preference for owner-occupants is critical to deter speculators who only contribute to neighborhood instability.

The Minnesota Housing Finance Agency demonstrated a unique way to use existing Federal HOME grants to create an opportunity from the foreclosure crisis. Minnesota Housing combined $9.2 million of HOME funding with other sources to create the HOME Homeowner Entry Loan

Program (a.k.a. HOME HELP). This program provides downpayment and entry assistance to first time homebuyers making at or below 80% of the area median income to purchase foreclosed properties. As of the end of 2009, 252 out of the 613 assisted loans went to the purchase of foreclosed homes in Minnesota. In Minneapolis, HOME HELP assisted a total of 69 loans, 23 were for purchases of foreclosed homes.

Conclusion

And so, thank you, Madame Chairwoman, for the opportunity to participate in today's hearing and for your continued leadership in supporting the Neighborhood Stabilization Program, efforts to preserve affordable rental housing and support for responsible community development.

I hope the information that I presented to you today provided you with a sense of the broader housing market dynamics and how those are playing out in the City of Minneapolis.

I am happy to answer any questions.